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No. _____

Supreme Court, U.S.
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IN THE
Supreme Court of the United States
OCTOBER TERM, 1986

UNICON PRODUCING COMPANY,
Petitioner,

v.

JICARILLA APACHE TRIBE,
DONALD P. HODEL, Secretary of the
United States Department of the Interior,
and STATE OF NEW MEXICO,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

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QUESTIONS PRESENTED

1. Whether, in the administration of Indian mineral leases, the fiduciary role of the Secretary of the Interior requires him to resolve every ambiguity in a regulation or lease in favor of the affected tribe, regardless of the original intent of the provision as evidenced by a long-standing administrative interpretation, and further requires him to make every discretionary choice in the manner that best serves the tribe's short-term financial interests.

2. Whether, based on a finding that the Secretary breached his fiduciary duty in making discretionary judgments about the royalties payable under Indian mineral leases, the innocent lessees can be held retroactively liable for additional royalties that the Secretary never directed them to pay.

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DONALD P. HODEL, Secretary of the
United States Department of the Interior,
and STATE OF NEW MEXICO,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

The Unicon Producing Company petitions for a writ of certiorari to review the judgment of the United States Court of Appeals in this case.[1]

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[1] In addition to those parties listed in the caption, the parties below included the Southland Royalty Co., the Southern Union Company, and the Exxon Corporation, which are filing separate petitions. The State of New Mexico sought unsuccessfully to intervene in the district court, and its unsuccessful appeal from that ruling was consolidated with the instant case in the Tenth Circuit.

Petitioner Unicon Producing Company (successor to Supron Energy Corporation) is a partnership composed of the Union Texas Exploration Co., Exploration Finance Co., and SNPI. Union Texas Exploration Co. is a subsidiary of the Union Texas Petroleum Corp. Exploration Finance Co. and SNPI are both wholly owned by KMI Continental, Inc.

OPINIONS BELOW

The *en banc* decision of the United States Court of Appeals for the Tenth Circuit, dated January 23, 1986, is reported at 782 F.2d 855 and reprinted here at page 1a of the joint appendix being submitted by petitioner and three separate petitioners.[2] A modification of this decision by the *en banc* court, dated June 18, 1986, is unreported, and reprinted here at page 18a of the joint appendix. The original panel decision in the Tenth Circuit, dated February 24, 1984, is reported at 728 F.2d 1555 and is reprinted here at page 21a of the joint appendix. The main opinion of the United States District Court for the District of New Mexico, dated November 5, 1979, is reported at 479 F. Supp. 536 and reprinted here at page 104a of the joint appendix.[3]

JURISDICTION

This Court's jurisdiction is invoked on the basis of 28 U.S.C. § 1254(1). The *en banc* decision of the United States Court of Appeals for the Tenth Circuit is dated January 23, 1986. A timely petition for rehearing filed by petitioner and two others was denied on April 15, 1986. A timely motion for modification filed by respondent Hodel was denied on June 18, 1986. Also on June 18, 1986, the court of appeals on its own motion supplemented the January 26 opinion. On July 2, 1986, Justice Byron White granted petitioner's application for an extension of time for filing this petition to and including August 13, 1986.

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[2] This joint appendix, filed by petitioner, the Exxon Corp., the Southern Union Co., and the Southland Royalty Co., is cited here as "J.A."

[3] The final judgment of the district court was entered on June 1, 1981. See J.A. 165a.

CONSTITUTIONAL, STATUTORY AND REGULATORY PROVISIONS INVOLVED

The primary regulatory provisions at issue in this case —25 C.F.R. pt. 211 and 30 C.F.R. pt. 221 (1981)—are reprinted in full in the joint appendix at pages 214a-278a. The Indian Mineral Leasing Act, 25 U.S.C. §§ 396a-396g, is set out in full in the joint appendix at pages 200a-203a.

STATEMENT

Petitioner seeks review of a decision of the United States Court of Appeals for the Tenth Circuit, sitting *en banc*, which required a significant change in the method used to calculate royalties paid to the Jicarilla Apache tribe ("the Tribe") by lessees producing natural gas on the Jicarilla reservation in New Mexico. The decision requires use of the particular royalty system that is most advantageous to the Tribe, despite the acknowledged ambiguity of the governing leases and Interior regulations, and despite a consistent history of contrary administrative interpretation and commercial assumptions spanning more than two decades. The court held that the Secretary of the Interior's fiduciary duty to the Tribe *requires* him to select, in every case, the interpretation of ambiguous language that most favors the Indians. It further held that any discretion provided to the Secretary under the governing regulations must always be exercised in such a way as to maximize the immediate profits of the Tribe. Having found a breach of these duties here, the court then held that the lessees, who had no role in the breach, could be forced not only to accept a new interpretation of the leases for the future, but also to pay the difference retroactively.

The leases involved here date from the early 1950s and authorize petitioner and several other lessees [4] to produce

[4] Two other lessees, the Exxon Corporation and the Southland Royalty Company, are filing separate petitions. In addition, a peti-

oil and gas on designated parts of the Jicarilla reservation. Under authority granted by the Indian Mineral Leasing Act, 25 U.S.C. §§ 396a-396g, the Secretary controlled every aspect of the lease arrangements. The leases themselves were in a form prescribed by the Secretary, and closely tracked the language of certain Interior regulations [5] while incorporating others by reference.[6] Each individual lease was initially approved by the Secretary. Since that time, petitioners, or their predecessors, have been producing natural gas and making regular royalty payments to the Tribe based on a fixed percentage of the "value" of the gas produced. Throughout this period, the exact method used to calculate these royalties was actively supervised by the Secretary.[7]

An understanding of the royalty issues raised here requires some familiarity with the alternate ways in which natural gas may be produced and sold. The gas produced on the Jicarilla reservation comes out of the well as "wet gas," which means that it contains not only the usual elements of "dry" natural gas—primarily methane —but also heavier "liquids" like butane, propane, and natural gasoline. Especially where the gas must be transported long distances by pipeline, these heavier elements are typically extracted first, and then sold separately. A producer of wet gas therefore has two choices: he can sell the wet gas for a single price to the owner of an

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tion is to be filed by the Southern Union Company, which formerly owned the Gas Company of New Mexico—the company which purchased and processed gas produced by all lessees on the Jicarilla reservation. Southern Union was required by the district court, as a third-party defendant, to indemnify the lessees for some of the excess royalties assessed against them. J.A. 165a-172a.

[5] 25 C.F.R. § 211.13 (formerly codified as 25 C.F.R. § 171.13).

[6] 30 C.F.R. pt. 206 (formerly codified as 30 C.F.R. pt. 221).

[7] As the district court put it in 1978, "Royalties have been paid by all defendants based upon a determination and billing by the Secretary." J.A. 68a.

extraction plant, or he can operate his own extraction plant and sell the constituent elements separately.[8]

Royalties to the owner of the land where wells have been drilled, in turn, can be calculated in two different ways. First, under the "BTU adjustment method," royalties are based on the value of the unprocessed wet gas produced by the lessee and sold at the wellhead. That value is a reflection of the volume of gas produced, the "BTU content" of the gas, and the prevailing price for sales of gas from the field. The alternative—called the "net realization method"—is based on the value of the several constituent elements of the gas after they have been extracted at a processing plant, minus an allowance for the costs of transportation and processing.[9]

The underlying issue raised in this lawsuit is the appropriate method for calculating the royalties payable to the Tribe by those lessees who simply sold the gas produced at the wellhead to third parties. From the execution of the leases until 1979, the Secretary approved the calculation of royalties by these lessees based on a percentage of the payments they were receiving under sales contracts for the wet gas. In effect, this meant that the royalties were based on some variant of the BTU-adjust-

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[8] As an economic matter, construction of an extraction plant is only feasible where large amounts of wet gas can be processed in one location. Here, there was only one processing plant that received gas produced by several different lessees both on and off the Jicarilla reservation.

[9] In theory, these two valuation approaches should produce roughly the same result, since the price paid for wet gas in the field should reflect the value of the constituent elements reduced by the cost of their transportation and extraction. But the results will not always be identical. In particular, they may vary where, as here, the prices paid for wet gas at the wellhead come from long-term contracts, while the prices paid for the constituent elements after processing are more variable. There is also some "shrinkage" of the gas between the wellhead and the processing plant.

ment method.[10] The net realization method, with its focus on the value of extracted elements, came into play only where a particular lessee itself owned an interest in a processing plant.[11]

Starting in 1973, however, the Tribe began arguing that the leases and regulations required "dual accounting" —*i.e.*, continuous calculation of the royalties under both methods, and payment of royalty under whichever system produces a higher result at any given time. Under this approach, the lessees would be required to maintain two separate accounting systems for royalties—one of which is based, not on their own sales figures, but on the prices received by their *customers* when those customers transport and process the wet gas and sell the component elements. This system would significantly increase the lessees' cost of operation, both because it would mean increased royalties during some periods and because it would more than double the burdens associated with accounting for royalty purposes.[12]

After trying unsuccessfully to convince the Secretary to impose dual accounting, the Tribe filed suit in 1975 against the Secretary and various lessees, including petitioner, seeking a change to the dual accounting system and an accounting for any deficiency caused by the Secretary's failure to impose this requirement in previous

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[10] It was only in 1974 that the sales contracts for wet gas produced by these lessees began to be based explicitly on BTU content. J.A. 132a. Prior to that time, the parties simply negotiated a price for a particular volume of gas produced.

[11] As Judge Seth noted in the court below, petitioner's predecessor was required to report and account for royalties on the dual accounting system during a period of time when it owned the processing plant. J.A. 25a.

[12] The system would also be illogical, because it would penalize lessees for the business acumen of their customers. The percentage of lessees' revenue going toward royalties would increase whenever the purchaser, who operates the extraction plant, made some especially favorable sales of his gas products or, through new investment, increased the operating efficiency of the plant itself.

years.[13] The defendants responded that the consistent interpretation given to the leases and regulations by the Secretary and the parties over many years foreclosed any suggestion that dual accounting was to apply to lessees who sold wet gas directly to third parties.

These competing positions were based on differing interpretations of the complex language contained in the leases and regulations. The lessees relied primarily on the basic definition in the leases of "value" for purposes of royalty calculations.[14] This definition appears to focus the issue on the particular product sold by the lessee, which in this case is the unprocessed wet gas. The Tribe countered this argument by pointing to a later passage in the same paragraph, and to an additional regulation,[15] both of which describe the mechanics of the dual accounting approach. It argued that these passages represent an endorsement of dual accounting for all lessees, rather than just for those lessees who operate their own extraction plants.

The district court initially favored the position of the lessees. In 1978, on motions for partial summary judgment, it held that there could be no retroactive reassessment of the "value" of the gas produced for royalty purposes, because the Secretary had validly exercised his discretion to compute value based on the actual price received by the lessees. J.A. 66a-69a. However in 1979, after a bench trial, the district court reversed course and ruled for the Tribe, holding that dual accounting is required of all lessees. J.A. 125a-135a. In so doing, the court relied primarily on its own analysis of the regulatory language. It also was influenced by the assumption that even if the

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[13] Federal jurisdiction was premised on 28 U.S.C. §§ 1331(a) and 1362.

[14] Lease ¶ 3(c) (reprinted in the regulations at 25 C.F.R. § 211.13(a)).

[15] 30 C.F.R. § 206.105(c).

leases granted the Secretary discretion to waive dual accounting, that discretion would necessarily be "circumscribe[d]" by the "Secretary's fiduciary obligation to the Tribe." J.A. 127. The court ordered an accounting to determine what further amounts might be owing, under the dual accounting system, for the period 1970 onward.[16]

The defendants appealed to the Tenth Circuit,[17] where the Secretary, for the first time, began arguing that the leases and regulations authorized him to impose dual accounting on all lessees.[18] The Secretary acknowledged that he had never imposed dual accounting on a lessee who did not operate an extraction plant, but noted that in August 1979 an Assistant Secretary had stated his intention to begin doing so "if the authority to do so is clarified." [19] He added that the legal basis for this new "policy" had been provided by a July 1981 opinion issued by the Department's Office of the Solicitor.[20]

On February 24, 1984, a three-judge panel of the Tenth Circuit reversed by a vote of 2-1. J.A. 21a. Judge Seth, writing for the majority, held that dual accounting is not required under the leases for lessees who sell wet gas to

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[16] In subsequent orders, the court considered several revised accountings by the Secretary of the amounts due and owing. Finally, on June 1, 1981, the court approved an accounting which provided for payments to the Tribe totalling $343,936 for the period 1970-79. J.A. 166a. At the same time, it ordered Southern Union to indemnify the lessees for a substantial portion of this amount. J.A. 166a-172a.

[17] The Tribe also appealed, raising several issues not pertinent here.

[18] *See* Reply Brief for the Sec'y, at 5-8 (May 1982).

[19] Supplemental Brief for the Sec'y, at 13 (July 1984) (quoting a Memorandum in Response to Court Order of April 11, 1979, in *Jicarilla Apache Tribe v. Conoco*, Civil No. 76-430 (D.N.M.)).

[20] *Id.* at 14. In fact, however, it is far from clear that the Secretary has actually implemented this policy change with respect to any leases outside the Jicarilla reservation. See note 34 *infra*.

third parties. He relied on the Secretary's original and long-standing interpretation of the leases, which he found to be reasonable and therefore sustainable. J.A. 29a. He also concluded that it could not be a breach of the Secretary's fiduciary duty for him to approve a method of royalty calculation that conforms both with the "general practices in the industry" and with the "controlling case law." J.A. 30a.

Judge Seymour dissented. Unlike the district court, she did not suggest that dual accounting was required by the plain language of the leases and regulations. She conceded that the Secretary's long-standing interpretation—limiting dual accounting to lessees who also owned extraction plants—was "reasonable." J.A. 48a. This was not, however, enough in her view to justify rejection of the Tribe's claim, since it is erroneous to employ normal "administrative law analysis without considering what role, if any, the Secretary's fiduciary duty should play in a court's examination of his administrative action." J.A. 44a. In her view, that fiduciary duty had two consequences here. First, it required the Secretary to interpret the ambiguous royalty terms in the leases and regulations in a manner favorable to the Tribe—*i.e.*, to find that he at least had the discretion to order dual accounting even for lessees who sold their gas at the wellhead. J.A. 44a. Second, the Secretary was required, as a fiduciary, to exercise this new-found discretion in the way most favorable to the Tribe's interests—*i.e.*, to require dual accounting of all lessees.[21] *Ibid.* Having reached the conclusion that this was the only "discretionary" choice available to the Secretary, Judge Seymour then agreed with the district court that the lessees should be financially re-

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[21] In fact, the distinction between the Secretary's *interpretation* of the regulations and his *exercise of discretion* is not as clear as it might be in Judge Seymour's opinion. The opinion seems to shift back and forth constantly between these two conceptually distinct issues. It is clear, however, that the opinion will be deemed controlling in later cases raising either issue.

sponsible for the Secretary's breach of fiduciary duty, even without a finding that they were aware of or participated in the breach of trust.

The Tribe's motion for rehearing *en banc* was granted and, on January 23, 1986, the Tenth Circuit, by a vote of 4-3, overruled the panel and affirmed the district court. The majority, in a short *per curiam* opinion, adopted the dissent of Judge Seymour with only slight modifications not pertinent here. J.A. 3a. Judge Seth, dissenting for himself and two others, repeated his argument that any fiduciary duty owed the Tribe by the Secretary was insufficient to justify overturning a reasonable interpretation of leases and regulations that had gone unquestioned for more than two decades. J.A. 5a.

On June 18, 1986, the Tenth Circuit denied the Secretary's motion to modify its decision, which had argued that the standard of fiduciary duty enunciated by the court was too stringent.[22] J.A. 18a. In so doing, the court *sua sponte* added a one-paragraph discussion of the lessees' claim that the Tribe's proper remedy was against the government. J.A. 18a-19a.

REASONS FOR GRANTING THE WRIT

This case raises important questions about the proper role of the federal government's "fiduciary duty" to Indians in the interpretation and administration of Indian mineral leases and regulations. In a well-intentioned but misguided effort to advance the interests of Indians, the Tenth Circuit has mandated two new requirements that would encroach on the legitimate authority of the Secretary, overturn the reasonable expectations of the lessees and, ultimately, harm the Indians themselves. Under this ruling, every perceived ambiguity in leases and regulations must be resolved in the way that is most favorable

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[22] On April 15, 1986, the court had already denied, with two dissenting votes, the lessees' petition for rehearing of the *en banc* decision. J.A. 15a.

to the affected Indians, even where years of consistent administration by the Secretary and commercial operation by the lessees counsel in favor of a different interpretation of the original intent. In addition, the Secretary is effectively prohibited from retaining any real discretion for himself in the administration of these leases, because every choice presented to him must be resolved in the way that maximizes the immediate profits of the tribe.

Such a complete suspension of the usual principles of administrative and commercial law cannot be justified under any valid theory of fiduciary obligations. While the Secretary may well have a "fiduciary" role to play in this field, that fact hardly requires him to ignore the original understanding of leases and regulations and choose the most "pro-Indian" interpretation of every phrase that now seems ambiguous. Nor can it transform every discretionary judgment reserved for the Secretary into a ministerial selection of the option that best serves the immediate interests of the Tribe.

The clear effect of these new rules is to authorize frequent judicial interference not only with the administration of several thousand oil and gas leases on dozens of reservations,[23] but also with many other interpretations and decisions made by the Secretary in his capacity as a

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[23] Indian oil and gas reserves exist on forty reservations in seventeen states. American Indian Policy Review Comm'n, *Final Report* 338 (1977). The Tribe stated in the court below that the panel decision would "directly and adversely affect over two thousand Indian oil and gas leases covering over two million acres of Indian lands held in trust by the United States for thirty-three Indian tribes." Reply Br. on Rehearing *En Banc*, at 1. Moreover, we note that Indian reservations contain a number of other commercially valuable mineral deposits. Senate Comm. on Interior and Insular Affairs, 94th Cong., 2d Sess., *Management of Indian Natural Resources*, pt. 2 (Comm. Print 1976) (report produced by the Comptroller General of the United States).

protector of Indian interests.[24] Private parties dealing with Indian tribes, in turn, will see the terms of their commercial relationships constantly made less advantageous, as new perceived ambiguities are all resolved in favor of the tribes and every discretionary judgment is made on the same basis. They then may be forced to pay retroactively for any delay by the Secretary in ordering these changes in the contractual arrangements. The likely result will be real disincentives to future dealings with Indians—to the ultimate detriment of the very people whom the Tenth Circuit was seeking to help.

I. The Secretary's Fiduciary Role in Indian Mineral Leasing Does Not Require Him to Resolve Every Ambiguity, and Make Every Discretionary Choice, in the Manner that Most Favors the Affected Tribe.

The importance of the concept of fiduciary duty in the reasoning of the court below cannot be overstated. As we have discussed, the court relied solely on this concept for two different holdings: first, that the leases and regulations had to be *interpreted* as allowing imposition of dual accounting on every lessee, and second, that the Secretary was required to *exercise his discretion* to impose dual accounting on every lessee. In fact, however, neither of these requirements is sustainable as a matter of law or justifiable as a means to protect the interests of Indians.

A. Fiduciary Duty and the Interpretation of Leases and Regulations

On the issue of royalty calculation, there are three plausible ways in which the controlling provisions in the leases and regulations could be interpreted. First, they might be interpreted as requiring that royalties paid by

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[24] *See, e.g., United States v. Mitchell*, 463 U.S. 206, 219-223 (1983) (describing pervasive governmental role in arranging terms of timber sales from Indian lands as well as rights-of-way across these lands).

those lessees who simply produce and sell wet gas be based on the volume and value of wet gas they produce—*i.e.*, the BTU adjustment method.[25] Second, they might be interpreted as calling for dual accounting by all lessees. Third, they might be interpreted as leaving the Secretary full *discretion* to decide whether to require dual accounting by lessees who produce and sell wet gas.

Unlike the district court, neither the majority nor the dissenters in the Tenth Circuit took the view that this interpretive question could be resolved based solely on the language itself. Where the two sides differed was on what additional factors should control the outcome. Judge Seth, in his original panel majority opinion and his later dissent, relied primarily on the fact that, from 1950 to 1979, the Secretary had consistently required lessees who sell wet gas to pay royalties based on a percentage of the price received for that product at the wellhead.[26] He saw this as a convincing demonstration that the leases and regulations never contemplated a requirement of dual accounting by those lessees who did not, themselves, process the wet gas into its constituent elements.[27]

By contrast, Judge Seymour, in the opinion that ultimately became controlling, expressly rejected reliance on the usual "administrative law" approach, with its require-

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[25] Under this interpretation, the language in the leases and regulations calling for dual accounting would be understood as applicable solely to those lessees who own extraction plants.

[26] He also noted that this was the consistent commercial practice in the private sector. J.A. 28a.

[27] Judge Seth noted the fact that the Secretary had, in 1979, begun stating that he had discretion to require dual accounting in such cases, but he gave no weight to this fact, viewing it as a "response to rulings on the point by the trial court during these proceedings." J.A. 29a. He might also have pointed out that an agency's interpretation that conflicts with its own earlier pronouncements is entitled to little weight. *See Skidmore v. Swift & Co.*, 323 U.S. 134, 140 (1944).

ment of deference to reasonable agency interpretations. J.A. 44a. While acknowledging that Judge Seth's interpretation was "reasonable," J.A. 48a, she stated that "the Secretary's actions in a situation such as this are constrained by principles of Indian trust obligations as well as by standards of administrative law." J.A. 44a. Relying both on the overall special relationship between Indians and the federal government and on the specific terms of the Indian Mineral Leasing Act, she asserted that a different interpretation of the regulations is mandatory if it too is "reasonable" and it "better promotes the Tribe's interest." J.A. 45a.

In reaching this result, the court below ignored not only the usual principles of administrative law governing interpretation of regulations, but also the black-letter law of contracts—which ought to have some role where the issue is the interpretation of leases controlling the rights of private parties. In both areas of the law, the process for construing ambiguous language is fundamentally the same: the court looks at surrounding circumstances in an effort to ascertain the original intent.[28] And one key indicator is a consistent interpretation given to the language by its author—here the Secretary.[29] Fiduciary

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[28] *Compare* 1 A. Corbin, *Contracts* § 106, at 476 (1963) ("It is certain that the purpose of the court is in all cases the ascertainment of the 'intention of the parties' if they had one in common.") *with* 2 K. Davis, *Administrative Law Treatise* § 7:22, at 107 (1979) ("deference is due the administrator's interpretation of a regulation, because the administrators are likely to know more about the *background of intent* that went into the regulation") (former emphasis omitted; new emphasis supplied).

[29] The administrative cases supporting this principle are legion. *See, e.g., Thorpe v. Housing Authority,* 393 U.S. 268, 276 (1969); *Udall v. Tallman,* 380 U.S. 1, 16-17 (1965). In contract cases, the issue is whether *both* parties shared an original understanding, and evidenced this understanding through consistent conduct under an existing contract. *See Reconstruction Finance Corp. v. Sherwood Distilling Co.,* 200 F.2d 672, 676 (4th Cir. 1952) ("the interpreta-

duty, we submit, is too slim a reed to justify a wholly different approach simply because this is an Indian case.

There are, to be sure, numerous decisions of this Court recognizing that " 'statutes passed for the benefit of dependent Indian tribes . . . are to be liberally construed, doubtful expressions being resolved in favor of the Indians.' " *Bryan v. Itasca County*, 426 U.S. 373, 392 (1976) (quoting *Alaska Pacific Fisheries v. United States*, 248 U.S. 78, 89 (1918)). *See also Antoine v. Washington*, 420 U.S. 194, 199-200 (1975); *McClanahan v. Arizona State Tax Comm'n*, 411 U.S. 164, 174 (1973). The same is presumably true when it comes to the interpretation of regulations. *See Jicarilla Apache Tribe v. Andrus*, 687 F.2d 1324, 1332 (10th Cir. 1982). These decisions reflect the fact that Indians have a unique legal and historical status, requiring special judicial solicitude.

But these cases do not even begin to justify the Tenth Circuit's total refusal to consider the traditional indicia of what these regulations and leases were actually intended to mean. After all, "it is one thing to say that courts should construe treaties and statutes dealing with Indians liberally, and quite another to say that, based on those same policy considerations . . . , courts themselves are free to create favorable rules" where other rules were actually intended. *Fry v. United States*, 557 F.2d 646, 649 (9th Cir. 1977), *cert. denied*, 434 U.S. 1011 (1978). *See also Andrus v. Glover Construction Co.*, 446 U.S. 608, 619 (1980) (this " 'canon of construction is not a license to disregard clear expressions of . . . congressional intent' ") (citation omitted). And there is nothing about the dependent status of Indians that forecloses a determination of actual intent based on sur-

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tion placed upon a contract by the parties themselves, before a dispute has arisen, is entitled to the greatest weight"); *Thompson v. Fairleigh*, 300 Ky. 144, 187 S.W.2d 812 (1945) ("There is an old saying of an English judge: 'show me what the parties did under the contract and I will show you what the contract means.' ")

rounding circumstances, such as a long and consistent administrative interpretation. *See Oliphant v. Suquamish Indian Tribe*, 435 U.S. 191, 208 n.17 (1978) ("treaty and statutory provisions which are not clear on their face may 'be clear from the surrounding circumstances and legislative history' ") (quoting *DeCoteau v. District County Court*, 420 U.S. 425, 444 (1975)); *Mattz v. Arnett*, 412 U.S. 481, 505 (1973) (same).

Indeed, it was just such a history of administrative interpretation that recently led this Court to interpret an ambiguous statute in a manner contrary to the interests of an Indian tribe, in *Mountain States Telephone and Telegraph Co. v. Pueblo of Santa Ana*, 105 S. Ct. 2587 (1985). There, the Court dealt with a 1924 statute that contained apparently conflicting provisions. The Court conceded that it could not reconcile all of the statutory language, *id.* at 2597 n. 27, but chose to follow the "uniform contemporaneous view of the Executive Officer responsible for administering the statute," *id.* at 2597.[30] In so doing, it *rejected* the argument that "[a]mbiguous language in Indian statutes . . . always has been construed in favor of restrictions on alienation." *Id.* at 2609 (Brennan, J., dissenting).

To the extent that the court below was relying on specific fiduciary obligations derived from the Indian Mineral Leasing Act, that argument is equally unavailing. Indeed, it reveals the absurdity of giving controlling weight to the concept of "fiduciary duty" in the interpretation of ambiguous regulations. Even assuming that the Secretary was acting here as a fiduciary for the Tribe, it is clear that *any* of the three possible rules on royalty calculation outlined above—(1) requiring dual accounting by all lessees, (2) requiring dual accounting only for lessees who own processing plants, or (3) leav-

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[30] The Court noted that the Secretary's contemporaneous interpretation is " 'entitled to very great respect.' " *Ibid.* (citation omitted).

ing it to the Secretary's discretion—would have been perfectly permissible under the statute.[31] It follows that a court has no basis for ignoring what it actually can discern about the Secretary's real intent. When it does so, it risks interfering with a considered policy judgment that the Secretary was free to make, and providing an undeserved windfall to the affected Indians, all because the Secretary failed to express his actual intent in language of sufficient clarity to foreclose a later revisionist interpretation.

In sum, the concept of fiduciary duty cannot become a pretext for disregarding all of the usual rules for construing administrative regulations or commercial contracts. It is only by following these usual rules that the court can hope to remain true to the legitimate administrative judgments of the Secretary, as well as the understanding of the parties at the time they entered into these commercial arrangements.

B. Fiduciary Duty and the Exercise of the Secretary's Discretion

The Tenth Circuit's reasoning is no more convincing when it comes to the issue of the Secretary's exercise of his discretion. As we have noted, in addition to concluding that the regulations and leases must be read as *allowing* the Secretary to impose dual accounting on all lessees, Judge Seymour also determined that the Secretary's fiduciary role *requires* him to make this choice. This ruling was based solely on the fact that dual accounting, by definition, maximizes the royalties owed to the Tribe. But there is no basis in the governing statute or the general law of fiduciary duty for requiring the Secretary always to select this single option.

First, nothing in the Indian Mineral Leasing Act mandates that the Secretary always maximize the short-term financial benefit to the Tribe under an existing

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[31] See § I.B. *infra*.

lease arrangement. While it was certainly part of the congressional purpose to "ensure that Indians receive 'the greatest return from their property,'" *Montana v. Blackfeet Tribe*, 105 S. Ct. 2399, 2404 n. 5 (1985) (quoting S. Rep. No. 985, 75th Cong., 1st Sess. 2 (1937)), that does not mean that the Secretary was deprived of all discretion in setting the royalty terms. In particular, he was not required to ignore the commercial context of these lease arrangements, and the potential long-term impact of an effort to maximize the immediate income of the Indians. He retained the discretion to determine that some other arrangement, while still providing a fair return to the Indians, would be more likely to attract and retain lessees.[32] *See Navajo Tribe v. United States*, 9 Cl. Ct. 227 (1985) (appeal pending).[33]

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[32] This would be a particular concern where the option that maximized short-term income was a substantial departure from the usual custom and practice in the industry. Potential lessees are clearly more likely to seek investments where the royalty terms, in conformance with industry practices, are based on the revenue actually received by the lessee. Judge Seymour, in her controlling opinion, stated that "industry practices" have no relevance to "the Secretary's interpretation of federal law." J.A. 43a. But this assertion neglects the basic principle of trust law that the care required of a fiduciary is that of an ordinary man transacting similar business with a view to results similar to those required by the trust. G. Bogert, *The Law of Trust and Trustee* § 541 (2d ed. 1978).

[33] In *Navajo Tribe*, the Tribe claimed that the Secretary had breached his fiduciary duty by not collecting rentals from companies prospecting on tribal lands. The Claims Court found that the requirement in the Indian Mineral Leasing Act that the Indians receive the "greatest return from their property" did not bind the Secretary merely to charging the highest possible price for every endeavor. The court held that while the Secretary might be able to obtain more in the short run by charging rental for non-Indians to prospect on tribal land, this would conflict with the usual practice in the industry and thus might discourage mining companies from prospecting on the reservation. This, in turn, "would serve to defeat the goal of insuring the greatest return from Indian property." 9 Cl. Ct. at 242.

In addition, even as he protected the right of the Tribe to be fairly paid for its mineral resources, the Secretary was authorized to give at least some consideration to other interests as well. The Congress has given the Secretary a long list of "public business" over which he has statutory authority. 43 U.S.C. § 1457. He has a broad duty to the public as a whole to manage natural resources for the general good. Thus, even where he is acting as a fiduciary for Indians, he is not foreclosed from weighing such goals as promoting energy exploration or national energy independence. *See North Slope Borough v. Andrus*, 642 F.2d 589, 612-13 (D.C. Cir. 1980) ("Of course, no one can claim that the interests of the Eskimoes, or of the environment for that matter, were an overriding veto staying the Secretary's hand with respect to other public concerns."); *cf. Nevada v. United States*, 463 U.S. 110, 128 (1983) ("The government does not 'compromise' its obligation to one interest that Congress obliges it to represent by the mere fact that it simultaneously performs another task for another interest that Congress has obligated it by statute to do.")

The recognition that the Secretary retained some discretion to choose among competing options, in turn, is consistent with the general principles that apply whenever the Secretary is acting as a fiduciary for Indians. *See, e.g., Moose v. United States*, 674 F.2d 1277, 1284 (9th Cir. 1982) (Secretary's duty to invest fund prudently does not create ministerial duties enforceable by mandamus). The applicable standard of judicial review leaves plenty of room for the exercise of discretion. As the Court of Claims put it, the appropriate standard is "not the court's or plaintiffs' own view of the preferable conduct," but the "normal standard for government fiduciaries—were their actions in good faith and within the realm of their acceptable discretion, or were they arbitrary, capricious, in abuse of discretion, or contrary to law?" *Mitchell v. United States*, 664 F.2d 265, 274 (Ct.

Cl. 1981) (*en banc*), *aff'd*, 463 U.S. 206 (1983). The actions of the Secretary will not be disturbed as long as he " 'exercise[s] such care and skill as a man of ordinary prudence would exercise in dealing with his own property.' " *United States v. Mason*, 412 U.S. 391, 398 (1973) (citation omitted). By this test, if the Secretary had the discretion under the leases and regulations to choose one of several royalty systems—all of which provided a fair return—he did not lose that discretion because of his fiduciary status.

C. The Consequences of the Tenth Circuit's Misunderstanding of Fiduciary Duty

In addition to being unjustified as a matter of law, the Tenth Circuit's understanding of fiduciary duties is both unfair to those who have contracted with Indians on terms set by the Secretary, and potentially harmful to the Indians as well. The most obvious concerns are raised by a rule that every ambiguous phrase in a lease or regulation must be interpreted in the manner most favorable to the Indian party. Because it prevents any inquiry into the actual intent of the parties as revealed by surrounding circumstances, such a rule essentially authorizes a court to rewrite the terms of a commercial deal long after it has gone into effect. Here, for example, as Judge Seth convincingly argued in the court below, nearly thirty years of consistent operation under these leases suggests that neither the Secretary nor anyone else ever intended to require dual accounting by lessees who did not own an interest in an extraction plant. Indeed, despite the Secretary's representations in the court below, from all indications it is still true that the Jicarilla reservation is the only place in the country where all lessees are being required to use dual accounting for royalties.[34] The court, however, paid no heed whatever

[34] As noted above, the Secretary has stated that the Department began favoring universal dual accounting in 1979 and found legal

to this evidence of actual intent, relying instead on the principle that the Secretary was bound to resolve every ambiguity in favor of the Tribe.

If applied generally, such an interpretive approach could have only one effect: deterrence of businesses from entering into commercial relationships with Indians under the supervision of the Secretary. Parties entering into major business transactions need to be confident that they understand the terms of the deal. They will be reluctant to enter into any contractual arrangement if there is reason to believe that a court may later refuse to be bound by clear indications of the parties' actual intent. And they will be particularly reluctant if they know that, in lieu of looking at intent, the court will apply one simple rule: the Indian interests always prevail. In sum, if the Tenth Circuit's ruling remains intact, many companies will begin looking for alternative commercial partners who, unlike the Indians, do not go into every dispute over contractual intepretation with an unfair presumption in their favor.

The same basic problems are raised by the court's second rule—that if the lease or regulation provides for the Secretary to exercise *discretion*, he must always do so in the way that most favors the Tribe. In such a case, of course, the other contracting party has accepted a measure of uncertainty with respect to how the deal will ultimately proceed. But that party has not agreed to an arrangement whereby *every* undecided issue that is left to the Secretary's "discretion" will necessarily be decided to its detriment. At the time the deal was struck, it had every reason to expect that these issues would be decided by the Secretary alone, based on his neutral assessment of fairness to all parties, the usual custom in the indus-

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authority for this policy in 1981. *See* p. 8 *supra*. However as Judge Seth noted in January, these apparently are the "*only* Indian or public land leases in the country where this construction is now applied." J.A. 12a (emphasis in original).

try, the National Interest, etc. By defeating this expectation, the decision below creates not only a second issue of fairness here, but also a second reason why companies will in the future be reluctant to enter into commercial ventures with Indians.

II. Even Assuming that the Secretary Breached His Fiduciary Duties, the Proper Remedy Was Not Retroactive Restitution From the Lessees.

Even if we assume that the Tenth Circuit was correct in holding that the Secretary breached his fiduciary duty to the Tribe by not directing that all lessees use dual accounting, that ruling would at most provide a basis for a change in the *current* operation of the leases. It would not justify the court's additional holding that petitioner and the other lessees must make *retroactive* royalty payments, reflecting the amount that they would have owed to the Tribe if the Secretary had not breached his duty. By choosing to impose the entire burden of the Secretary's alleged breach on innocent third parties, the court below added an entirely new and even more serious element of unfairness to its already questionable ruling.

In assessing this issue, it is important to recall how the royalty payments made by the lessees over the years were set. Every detail of the royalty payments resulting from these leases was supervised and approved by the Secretary, as required by the leases themselves. The lessees, in turn, complied fully with the Secretary's requirements, as they were then understood. At trial, it was stipulated that "defendants accurately reported the volumes of gas produced from the leases and the prices received on sales of such gas at the wellhead and that defendants accurately paid royalties based on the volumes and prices reported." [35] J.A. 126a.

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[35] It was on this basis that the district court, while finding that the lessees breached their obligations, nevertheless added that it was "through no apparent fault of their own." J.A. 127a.

Despite these facts, both the district court and the Tenth Circuit held that the lessees were responsible for back royalty payments. Both courts reached this result simply by asserting that any breach of fiduciary duty by the Secretary in his supervision and control of royalty payments necessarily led to a breach of contract by the lessees.[36] But this was far from a sufficient justification.

To begin with, it is black-letter law that a trust beneficiary injured by his fiduciary's breach of trust does not generally have a remedy against a third party. Restatement (Second) of Trusts § 284 (1959).[37] Instead, he must seek relief directly against the fiduciary. *Id.* §§ 205-212. The only exception is where the third party had notice of the breach and participated in it. *Id.* § 284; *see United States v. Dann*, 105 S. Ct. 1058, 1064-65 & n. 11 (1985). Thus, while noting this narrow exception, Professor Scott adds that it is "quite a different matter . . . to compel [third parties] to supervise the conduct of the fiduciary and to hold them liable for failure to do so." A. Scott, *The Law of Trusts* § 326.6 (2d ed. 1956). A general rule imposing such liability on third parties would make it "dangerous to deal with a fiduciary" as

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[36] In the district court's words, "If the Secretary has breached his fiduciary duty . . . , then the defendants have in fact breached the terms of the lease." J.A. 126a-127a. The Tenth Circuit agreed: "The failure of the Secretary to require dual accounting resulted in the lessees paying an insufficient amount of royalties under the contract." J.A. 19a.

[37] *See United States v. Dann*, 105 S. Ct. 1058, 1064 (1985) (third party not liable where he makes payment to trustee for benefit of beneficiary, and has no notice that trustee will misappropriate funds); *Holly v. Domestic and Foreign Missionary Society*, 180 U.S. 284 (1901) (third party not liable where it receives funds from attorney without notice that attorney has misappropriated them from account of client); *Paolino v. Channel Home Centers*, 668 F.2d 721 (3d Cir. 1981) (retailer not liable for marketing product until he had notice that manufacturer had appropriated the design for its own benefit in breach of duties to inventor with whom it had relationship of trust and confidence).

well as "seriously interfer[ing] with the proper performance by the fiduciary of his duties." *Ibid.*

These general principles are fully applicable in cases involving the Secretary's fiduciary obligations to the Indians. Three years ago, in *United States v. Mitchell*, 463 U.S. 206 (1983), this Court described at some length the legal basis for holding the United States liable in damages for the Secretary's alleged breach of trust in the management of Indian timber resources. *Id.* at 226-27. It saw no basis for creating an exception to the usual rule that an injured beneficiary has a right to "sue the trustee for damages resulting from a breach of the trust." [38] *Id.* at 226. By contrast, that same Term, the Court rejected a claim that a tribe injured by an alleged breach of trust by the Secretary could sue the party who benefited from the breach. In *Nevada v. United States*, 463 U.S. 110, 144 n. 16 (1983), the Court stated that "[i]f, in carrying out its role as representative, the Government violated its obligations to the Tribe, then the Tribe's remedy is against the Government, not against third parties." [39]

As we have noted, however, the Tenth Circuit refused to accept these basic principles, choosing instead to hold

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[38] *See also Gila River Pima-Maricopa Indian Community v. United States*, 684 F.2d 852 (Ct. Cl. 1982) (*per curiam*) (United States held liable for allowing upstream diversions of water by third parties).

We note that the Tribe has filed just such a claim in the Claims Court. *Jicarilla Apache Tribe v. United States*, No. 112-77 (Cl. Ct.) (proceedings stayed pending the outcome of the present action).

[39] This same principle was followed in *Duncan v. Andrus*, 517 F. Supp. 1 (N.D. Cal. 1977), where the court held that the government had breached its fiduciary duty in terminating federal supervision and control of particular Indian lands. The court was careful, in ordering relief, to protect the "rights of third party non-Indian good faith purchasers [who] may have taken record title without knowledge of the intricacies of the fiduciary obligations of the Secretary and any resulting ownership defects." *Id.* at 6.

the lessees—innocent parties who merely complied with Secretary's existing requirements—retroactively liable for additional royalties. In so doing, it sought to distinguish the *Nevada* decision on the ground that it involved a breach of trust by the Secretary representing a tribe in litigation, resulting in a foreclosure of rights as *res judicata*, whereas here the Secretary's "breach" occurred in a contractual context. J.A. 19a.

This theory might make some sense if, as the district court held, the Secretary's real failure was a misapplication of the plain requirements of the leases signed by the lessees and the Tribe. In such a case, it might be fair to hold the lessees to the clear terms of the deal they signed.[40] But it is quite another matter to hold the lessees responsible for the Secretary's failure to select a particular royalty system here, since even the Tenth Circuit did not suggest that dual accounting was mandated by the language of the leases.

Instead, as we have noted, the court below reasoned that the leases left the Secretary *discretion* to select one of several royalty schemes, and that he was required to choose dual accounting only because of a fiduciary duty arising from a statute or from the general principles governing relations between the United States and the Indians. Put differently, the only contractual obligation incurred by the lessees here was to pay the royalties specified by the Secretary. His misconduct, in turn, was the selection of a royalty method that conflicted with duties arising totally outside the contracts themselves. In

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[40] This was essentially the situation presented in the one case cited by the Tenth Circuit. *See Atlantic Richfield Co. v. Hickel*, 432 F.2d 587, 592 (10th Cir. 1970). There, federal agents had determined that a company owed the United States a particular royalty for oil and gas it had produced, whereas in fact a higher royalty was flatly required by statute. The court held that the errors of the agents did not alter the statutory right of the government to receive the higher royalty.

such a case, there is no basis for claiming that the Secretary's "breach" of his duties automatically caused a corresponding "breach" of the leases by the lessees.

To be sure, the Tenth Circuit's ruling might have something to recommend it if there were reason to believe that the lessees have received some sort of windfall from the Secretary's actions. But precisely the opposite is true. First of all, it is clear that the lessees have already paid full royalties on the gas they produced, on the same basis that would generally be used in the industry as a whole. More fundamentally, the lessees are now being asked, after the fact, to pay retroactive royalties calculated on a different basis. If the Secretary had recognized his alleged obligation to demand these higher royalties from the beginning, then this added "cost of doing business" could have been considered in the lessees' business planning. It might have affected the bids and bonuses they offered on the leases, or other significant strategic decisions. But none of this was possible here, because the Secretary failed to demand dual accounting for more than two decades.

Here again, in its effort to protect the interests of the Tribe, the Tenth Circuit has created a rule that may well end up deterring future commercial dealings with Indians. Under this decision, a lessee that attempts to comply in good faith with its contractual obligations, in the manner directed by the Secretary, may nevertheless be incurring a huge potential liability. Such a liability may be assessed whenever a court believes it has found an ambiguity in a lease or regulation, or a discretionary choice, that the Secretary should have resolved differently. And there is nothing that the lessee can do to minimize this risk, other than continually monitoring the Secretary's actions to make sure that every interpretation and discretionary decision is made in the way least favorable to the lessee's own financial interests. There can be no justification for asking businesses like petitioner to operate on that basis.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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